

The State of Illinois taxes leases differently for Retailers' Occupation Tax and Use Tax purposes than the majority of other states. See 86 Ill. Adm. Code 130.220. (This is a GIL).

September 15, 1999

Dear Mr. Xxxxx:

This letter is in response to your letter dated May 21, 1999. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter, you have stated and made inquiry as follows:

I am writing to you on behalf of one of my clients who is requesting a General Information Letter (GIL), pursuant to 2 Ill. Admin. Code Sec. 1200.120. The GIL should address whether our client is liable for Retailers' Occupation Tax (ROT) on its business transactions. GILs respond to inquiries made by taxpayers or their representatives. We understand that GILs discuss tax principles or applications and are not binding on the Illinois Department of Revenue (IDOR).

FACTS

1. The Business Organization

A grantor trust is in the auto-leasing business. Its owner/trustee utilizes an agent (XYZ) to manage the business. The agent does the billing, purchasing, and collecting for the trustee. It also holds title as agent to all leased vehicles. The trust has one investor/beneficiary who contributes funds to it. The trustee, through its agent, then uses the funds to finance auto-leasing transactions.

2. The Auto-Leasing Transaction

The auto-leasing transaction has the following steps:

- A customer wants to lease a new car, which is titled to a car dealer. The dealer purchased the car tax free by issuing to the car manufacturer an Illinois resale certificate.
- The car dealer sends the customer's credit application to the agent's office.

- Once the agent approves the application, the customer signs a lease agreement with the dealer as lessor.
- The lease is always for a term greater than one year. It is a true lease and not a conditional sale.
- The lease agreement clearly states that the dealer/lessor will immediately assign the lease to XYZ.
- The dealer is registered with the IDOR as a retailer.
- The dealer collects, under contractual agreement with the customer/lessee, sales tax measured by the car's selling price and remits the tax to the state.
- XYZ as agent for the trustee uses the trust's capital to purchase the car for its selling price.
- The car gets titled to "XYZ as agent" of the trustee, and the agent obtains from the Secretary of State certificate of title to the car.
- The dealer assigns the lease to XYZ which reassigns it to the trust.
- The trustee, through its agent, receives the stream of lease payments from the customer/lessee and then remits the payments to the investor/beneficiary.
- If the customer/lessee chooses to buy the car at the end of the lease, it pays to the agent the buyout amount which approximates the car's current fair-market value. (Alternatively, the buyout amount might be a pre-established fixed-price purchase option measured by a current estimate of the car's end-of-lease fair-market value.)
- The agent, which is an IDOR-registered retailer, collects sales tax on the buyout amount and remits it to the state.
- If the lessee/customer does not choose at the end of the lease to purchase the car, the agent sells it to an auction house. The agent obtains at point of sale the auction house's Illinois resale certificate. The auction house then sells the car to another dealer.

3. Sale of an Interest in the Trust

A beneficiary/investor may sell its interest in the trust. When a sale of an interest occurs, the identity of the beneficiary changes. However, title to and ownership of the leased cars remain with XYZ as agent for the trustee. Moreover, XYZ continues to manage the leases, which remain with the trust. The customer/lessee remains the same,

and it likewise retains its option to buy the automobile at the end of the lease for fair-market value. In other words, when a sale of an interest occurs, except for a change in the beneficiary/investor of the trust, the leasing business continues as usual.

ISSUES

Is sales tax imposed when the beneficiary sells its interest in the trust?

Since the dealer is initially listed as lessor on the lease agreement, do the subsequent assignments of the lease, first to XYZ as agent for the trustee and then to the trust, result in imposition of sales tax?

LAW

Illinois imposes the Retailers' Occupation Tax (the ROT) on persons selling at retail tangible personal property. 35 ILCS 120/2. "Sale at retail" is defined as the transfer for consideration, and not for resale, of title to or ownership of tangible personal property. 35 ILCS 120/1. Illinois also imposes the use tax (the UT) on the privilege of using in the state tangible personal property purchased anywhere at retail. 35 ILCS 105/3. The UT compliments the ROT. 86 Ill. Admin. Code Sec. 150.101(c). An IDOR regulation states that the ROT does not apply to sales of intangible personal property. 86 Ill. Admin. Code Sec. 130.120(a). The regulation cites evidences of interests in property as examples of intangible personal property. The IDOR has also stated that the sale of an interest in a trust, without a corresponding transfer of tangible personal property, is a sale of intangible personal property not subject to the ROT. GIL ST 94-0537 (11/7/94), and PLR ST 96-0424 (10/16/96). Furthermore, assignments of leases, without an accompanying transfer of tangible personal property, are considered sales of intangible personal property exempt from the ROT. PLRs ST 90-0232 (5/29/90), 90-0573 (7/31/90), and 96-0424 (10/16/96).

Illinois imposes the UT upon lessors because they are considered the end users of tangible personal property purchased for lease. 86 Ill. Admin. Code Sec. 130.220 (a) and 130.2010(b). Trusts in Illinois are subject to the UT if they are in the business of leasing tangible personal property in the state.¹ Dealers, which sell cars to trusts, along with assigning auto leases to them, are liable accordingly for the ROT on the selling price of the car.² PLRs ST 91-0372 (5/13/91), 93-0510 (8/6/93), and 96-0424 (10/16/96).

A lessor will owe at the end of the lease ROT on the buyout amount if it sells the car to the lessee. It will not owe ROT if it sells the car for resale and obtains at point of sale from the buyer a properly-

executed resale certificate. 35 ILCS 120/1(c), 86 Ill. Admin. Code Sec. 130.1405, and PLR ST 91-0372 (5/13/91).

The Illinois Secretary of State issues a certificate of title to a car only when it is satisfied that no ROT or UT is due on the vehicle. 625 ILCS 5/3-106, and GIL ST 94-0190 (6/13/94).

ANALYSIS

Applying the facts in the current case to state law, the sale of a beneficial interest in the trust would be exempt from the ROT because a transfer of title to or ownership of tangible personal property does not accompany the sale. In other words, when the beneficiary sells its interest in the trust, the leased vehicle remains titled to the agent of the trustee. Thus, the sale is one of intangible personal property not subject to the ROT. Likewise, the assignment of the lease from the agent of the trustee to the trust is exempt from ROT because no transfer of title to or ownership of tangible personal property accompanies the assignment. Therefore, it is considered a sale of intangible personal property exempt from the ROT.

ROT is due when the dealer assigns the lease agreement to the agent. This is because a transfer of title to and ownership of the vehicle accompanies the assignment. The dealer does pay the ROT due the IDOR.³ Further, the Secretary of State has acknowledged in effect that ROT/UT has been properly paid when it has allowed certificate of title to be issued to the agent. Finally, the agent would collect UT from the lessee/customer should it decide to buy the car at the end of the lease. The taxable base would be the buyout amount. However, no UT would be due from the purchaser if it tendered at point of sale a properly-completed Illinois resale certificate.

CONTRARY AUTHORITY AND DISCUSSION

The sale of the beneficial interest in the trust would only result in a taxable event if the beneficiary transferred tangible personal property along with the sale of the interest. However, under the facts as stated, no tangible personal property is conveyed when the beneficial interest of the trust is sold. There is likewise no taxable event when the agent assigns the lease to the trust, as no tangible personal property accompanies the assignment.

The dealer's initial execution of the lease and then its assignment to the agent may be considered two distinct taxable events. In other words, the dealer, as the initial lessor, might incur one UT and the agent, as the subsequent lessor, might incur another UT. However, several arguments to the contrary might be advanced: (1) The dealer upon executing the lease immediately assigns it to the agent, thereby

effectively avoiding for the car an intervening, and hence taxable, use. (2) Under similar circumstances, the IDOR has looked to the assigned lessor - whose name is pre-printed on the lease document and in whose name the property becomes titled - as the true lessor upon whom UT is due. (3) The Secretary of State has issued to the agent title to the car, acknowledging thereby that no additional UT is owed on the transaction.

CONCLUSION

The facts of this case support the finding that the sale of the beneficial interest in the trust would be a sale of intangible personal property beyond the scope of the ROT/UT. The transfer of the lease from the agent to the trust would also be exempt as the transfer of intangible personal property. Both conclusions are consistent with state law and prior IDOR rulings.

The facts of this case also support the finding that the dealer and the agent meet their respective ROT/UT obligations on the lease transaction when the dealer remits ROT to the state based on the selling price of the car. This conclusion is also consistent with state law and prior IDOR rulings.

We request that the IDOR send to us on behalf of our client a GIL addressing the issues presented. Your cooperation is appreciated.

For purposes of responding to your question, we are assuming that the grantor trust referenced in your letter is a valid trust operating under the Illinois Trust and Trustees Act. 35 ILCS 760/1 et seq. (1996 State Bar Edition). Further, we are also assuming that the trust, and not the trustee's agent, is the legal owner of the leased vehicles. The Department considers a trust authorized under the Trust and Trustees Act to be subject to the Retailers' Occupation Tax Act and the Use Tax Act if it is in the business of leasing tangible personal property in Illinois. Please note that the State of Illinois taxes leases differently for Retailers' Occupation Tax and Use Tax purposes than the majority of other states. For Illinois sales tax purposes, there are two types of leasing situations: conditional sales and true leases.

A conditional sale is usually characterized by a nominal or one dollar purchase option at the close of the lease term. Stated otherwise, if lessors are guaranteed at the time of the lease that the leased property will be sold, this transaction is considered to be a conditional sale at the outset of the transaction, thus making all receipts subject to Retailers' Occupation Tax.

A true lease generally has no buy out provision at the close of the lease. If a buy out provision does exist, it must be a fair market value buy out option in order to maintain the character of the true lease. Lessors of tangible personal property under true leases in Illinois are deemed end users of the

property to be leased. See the enclosed copy of 86 Ill. Adm. Code 130.220. As end users of tangible personal property located in Illinois, lessors owe Use Tax on their cost price of such property. The State of Illinois imposes no tax on rental receipts. Rental charges for a sublease are also not subject to tax in Illinois. Consequently, lessees incur no tax liability.

Please note that Under Illinois law, lessors may not "pass through" their tax obligation on to the lessees as taxes. However, lessors and lessees may make private contractual arrangements for a reimbursement of the tax to be paid by the lessees. If lessors and lessees have made private agreements where lessees agree to reimburse lessors for the amount of the tax paid, then lessees are obligated to fulfill the terms of the private contractual agreements.

The above guidelines are applicable to all true leases of tangible personal property in Illinois except for automobiles leased under terms of one year or less, which are subject to the Automobile Renting Occupation and Use Tax found at 35 ILCS 155/1 et seq. The Automobile Renting Occupation and Use Tax Act imposes a tax upon persons engaged in this State in the business of renting automobiles in Illinois under lease terms of one year or less at the rate of 5% of the gross receipts from such business. See the enclosed copy of 86 Ill. Adm. Code 180.101. Subsection (b) of Section 180.101 defines the term "automobile" for purposes of the Act and does not include commercial trucks, tractors, or trailers. Lessors of these types of vehicles are subject to Use Tax liability as discussed above.

If leases (not subject to Automobile Renting Occupation and Use Tax) are executed between the vehicle dealers, as lessors, and the applicants, as lessees, the dealers are acting as lessors of the leased vehicles. Absent a valid exemption, the dealers incur Use Tax liability based on their cost price of those vehicles. Since the dealers are considered the end users of the vehicles and incur the Use Tax, no Retailers' Occupation Tax is imposed upon the lease receipts and the lessees incur no Use Tax liability for the lease charges.

Since the dealers are considered to be purchasing the vehicles for their own use, those vehicles are not being purchased for resale. If the dealers do not know at the time of purchase of a specific vehicle whether it is to be resold or leased, the dealers may provide a blanket Certificate of Resale to the manufacturer. See subsection (c) of the enclosed copy of 86 Ill. Adm. Code 130.1405. However, when it is determined that the vehicle is going to be leased instead of resold, the dealers must self assess the appropriate amount of Use Tax on the cost price of the vehicle and remit that amount directly to the Department. If a dealer is able to determine that a given percentage of all purchases from a given manufacturer will be made for purposes of resale, the manufacturer may accept a blanket Certificate of Resale stating that a designated percentage of the sales made by the manufacturer to the dealer will be made for purposes of resale. See subsection (c) of 86 Ill. Adm. Code 130.1405.

Any person who is engaged in the business of leasing or renting motor vehicles to others and who, in connection with that business sells any used motor vehicle to a purchaser for his use and not for the purpose of resale, is making a

retail sale of that motor vehicle. See 35 ILCS 120/1c (1994 State Bar Edition). When a dealer sells a leased vehicle (whether under lease at that time or after the lease has ended) to the lessee or another person or entity, including a trust, those sales are sales at retail and are subject to Retailers' Occupation Tax liability on the gross receipts from such sales. Please see the enclosed copy of 86 Ill. Adm. Code 130.111. The Illinois purchasers incur the corresponding Use Tax liability, unless the vehicles are being purchased for resale.

Please note that, absent a valid exemption, there are two separate taxable transactions as described above when a dealer leases a vehicle and then sells or "assigns" that vehicle to another entity. Use Tax would be due on the use of the vehicle for lease and Retailers' Occupation Tax/Use Tax is due on the subsequent sale or transfer of the vehicle. None of the arguments presented in your letter, including those under the heading of "Contrary Authority and Discussion," affect this analysis. However, please be aware that when a vehicle dealer executes a lease with a customer for a vehicle (first taxable transaction) and the dealer contemporaneously sells that vehicle to another person or entity (second taxable transaction), the interim use exemption may apply to the first transaction (Use Tax liability that is incurred by the dealer on the cost of the vehicle that is used for leasing purposes). See the enclosed copy of 86 Ill. Adm. Code 150.306. This exemption may be available if the dealers are not primarily engaged in the business of leasing. The leasing of tangible personal property by persons who are primarily engaged in the business of selling such property at retail is within the interim use exemption if that tangible personal property is carried as inventory on the books of the retailer or is otherwise available for sale during the lease period. See the enclosed copy of 86 Ill. Adm. Code 150.306 (a)(2). Generally, motor vehicle dealers who enter into leases of motor vehicles under the above circumstances in order to make a contemporaneous sale of those vehicles may claim the interim use exemption. The dealer will incur Retailers' Occupation Tax liability on the second taxable transaction (sale of the leased vehicle) and the purchaser will incur Use Tax on the purchase price of the leased vehicle. See the enclosed copy of 86 Ill. Adm. Code 130.111.

The transfers or assignments of leases are considered transfers of intangible personal property. The Retailers' Occupation Tax Act and Use Tax Act only impose taxes with respect to transfers of tangible personal property. The transfers of leases without the transfer of the ownership of the leased property generally do not result in any Retailers' Occupation Tax or Use Tax liability. See subsection (a) of the enclosed copy of 86 Ill. Adm. Code 130.120. Please note that no deduction from Retailers' Occupation Tax liability will be permitted for any value attributable to intangible property or rights transferred in a sale of tangible personal property at retail if there is not clear evidence from the books and records of the retailer that the sale of such intangible property has been contracted for separately from the sale of the tangible personal property. See subsection (c) of the enclosed copy of 86 Ill. Adm. Code 130.220. If the dealers' books and records clearly establish that the sale of the leases have been contracted for separately from the sale of the vehicles, the gross receipts

from the sale of those leases will not be subject to Retailers' Occupation Tax liability.

As stated above, Retailers' Occupation Tax and Use Tax liability is only incurred on the transfer of tangible personal property. If no tangible personal property (including any leased vehicle) is transferred as part of the transfer or sale of a beneficial interest in a trust and the trust continues to be the owner of that property, no Retailers' Occupation Tax or Use Tax liability would be incurred on the gross receipts received from the transfer or sale of any of the beneficial interest in the trust.

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b).

Very truly yours,

Terry D. Charlton
Associate Counsel

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Enc.

¹ In cases wherein the assigned lessor's name appears preprinted on a leasing contract signed by the dealer, and wherein the car subsequently gets titled in the name of the assigned lessor, the IDOR has looked to the assigned lessor, rather than the dealer, as the true lessor. PLR ST 93-0510 (8/6/93).

¹ The auto dealer may reimburse itself for any ROT which it remitted to the IDOR by collecting UT from the customer/lessee (rather than from the trust). The dealer may collect the UT provided that it has contracted with the customer/lessee to do so. (The customer/lessee's obligation to pay the UT in this case is based on a contractual agreement with the dealer. Regardless of the contractual agreement, the dealer still remains legally obligated to remit the ROT to the state. Ibid.)

¹ The dealer may reimburse itself for the ROT due with the UT paid under contractual obligation to it by the customer/lessee. The dealer need not collect